

Supreme Court, U.S.

F I L E D

SEP 20 1991

No. 90-1029

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In The

Supreme Court of the United States
October Term, 1991

EASTMAN KODAK COMPANY,

Petitioner,

v.

IMAGE TECHNICAL SERVICES, INC., et al.

Respondents.

**On Writ Of Certiorari To The United States
Court Of Appeals For The Ninth Circuit**

**BRIEF AMICUS CURIAE OF
GRUMMAN CORPORATION
IN SUPPORT OF RESPONDENTS**

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IMAGE TECHNICAL SERVICES, INC., et al.*Respondents.***On Writ Of Certiorari To The United States
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IN SUPPORT OF RESPONDENTS****INTEREST OF AMICUS CURIAE¹**

Grumman Corporation, a leading U.S. defense contractor based on Long Island, New York, employs over 24,000 people. It both purchases and vends substantial amounts of computer maintenance. Grumman's operations are classified into four business segments: (1) aerospace - including the design and production of military

¹ Counsel of record to the parties in this case have consented to the filing of this brief, and letters of consent have been filed with the Clerk pursuant to Rule 37 of the Rules of this Court.

aircraft, space systems and commercial aircraft components; (2) electronics systems - including sophisticated electronics for aircraft, computerized test equipment and other defense-related products such as the joint STARS airborne surveillance system, utilized by the United States in the Gulf War; (3) special purpose vehicles - including fabrication of long life vehicles for the U.S. Postal Service, aluminum truck bodies and emergency vehicles; and (4) information and other services - including data systems operation and technical services which provide support for the U.S. space shuttle program and Grumman aircraft.

Grumman's defense and commercial operations are computer intensive. Grumman is both a customer and seller of computer support services. In the early 1970s, to support its computer-based operations, Grumman's Data Systems operation developed a computer maintenance division. Grumman has saved considerable expense as a result of servicing its own computers. Having developed this capability, Grumman later began to offer computer maintenance and other computer support services on a commercial basis to other computer users. Grumman Systems Support Corporation provides support services to users of a number of different brands of computer hardware and is now ranked as one of the largest independent service organizations ("ISOs") in the United States.

Grumman Systems Support Corporation is presently engaged in a litigation against a computer manufacturer which involves the same issue as presented in this case.²

² *Data General Corporation v. Grumman Systems Support Corporation*, No. 88-0033-S (D. Mass., filed March 28, 1988).

Grumman believes that the market definition standard utilized by the Court of Appeals in this case is both correct and consistent with the standards established by this Court. Markets should be defined through factual investigation, not by fiat. Grumman is submitting this brief *amicus curiae* because reversal of the decision of the Court of Appeals threatens Grumman's national defense and commercial operations. Without enforcement of the antitrust laws over the markets for high technology parts and support services³, Grumman's access to high quality, cost-effective computer support services for its defense, space and commercial activities will be endangered. Likewise, such a result will prevent Grumman from providing similar high quality, cost-effective computer support services on a commercial basis to other U.S. businesses.

Reversal would legalize a manufacturer's exercise of monopoly power in parts and service markets merely because the manufacturer has limited market power in the product sales market. Grumman believes that the better rule is to encourage competition in all markets.

SUMMARY OF ARGUMENT

The decision of the Court of Appeals correctly recognizes the legal viability and economic importance of competitive markets for the sale of high technology support services and spare parts. Allowing for the existence of

³ The legal analysis is the same for any high technology product, be they copiers, computers, medical imaging equipment, etc.

such markets separate from high technology product sales markets conforms with this Court's longstanding practice to look to the availability of substitutes in defining a market. Rejecting economic analysis and holding that market power for support services can never exist absent product sales market power would discourage competition in high technology service and parts markets to the detriment of Grumman and other service providers and consumers.

ARGUMENT

It is increasingly common practice in high technology industries for manufacturers, who once welcomed parts or service providers for their products, to impose new policies designed to eliminate competition in support service and spare parts sales markets. The respondents in this case, independent service organizations (ISOs) who specialize in servicing Kodak photocopy and micrographic equipment, challenged Kodak's attempt to alter the service market by implementing a new policy of refusing to sell replacement parts for Kodak equipment to ISOs or consumers who preferred to obtain support services from ISOs rather than Kodak. A question of fact was raised whether Kodak's change of policy lacked a competitive business justification and was intended, instead, to exclude competition for the service of Kodak equipment. The Court of Appeals' market analysis was proper.

I. THE DECISION OF THE COURT OF APPEALS CONFORMS WITH THE LONGSTANDING PRACTICE TO LOOK TO THE AVAILABILITY OF SUBSTITUTES IN DEFINING A MARKET.

Relevant antitrust markets have always been defined by this Court through factual investigation. *United States v. E.I. duPont de Nemours & Co.*, 351 U.S. 377 (1956); accord *Maple Flooring Mfrs. Ass'n v. United States*, 268 U.S. 563 (1925); *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); *United States v. Grinnell Corp.*, 384 U.S. 563 (1966). "Each case arising under the Sherman Act must be determined upon the particular facts disclosed by the record. . . ." *duPont*, 351 U.S. at 395 (quoting *Maple Flooring*, 268 U.S. 563).

In *duPont*, the leading case on market definition, this Court looked to the existence of substitutes to determine the product dimension. Under *duPont*, a "market is composed of products that have reasonable interchangeability for the purposes which they are produced - price, use, and qualities considered." *duPont*, 351 U.S. at 404. Application of this analysis may lead to a finding of a narrow, relevant market or "submarket" within a larger market: "there may be submarkets that are separate economic entities." *Grinnell*, 384 U.S. 563, 572. The boundaries of a submarket are determined by "examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes and specialized vendors." *Brown Shoe*, 370 U.S. 294, 325.

In the present case, respondents argued the existence of a market for support services. The Court of Appeals found that respondents offered sufficient evidence to satisfy the market definition requirements. Petitioner erroneously argues that service and spare parts sales markets cannot exist separate from product sales markets as a matter of law. To the contrary, such markets are both legally and economically sound.

Providing support services for high technology products is typically a brand-specific task requiring extensive training and inventory which is not transferrable to the maintenance and support of other manufacturers' high-technology products. Providing competitive support services to a specific manufacturer's products constitutes interbrand competition because competing service providers are offering their own brand of service for the product. The competitors offer different levels of service and different terms and conditions. Because Grumman and Data General, for example, are competitors for the "same generic product," i.e., support services for Data General equipment, they are engaged in interbrand competition. See *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 52 n.19 (1977). Such interbrand competition is protected by the antitrust laws.

In practice, the supply and demand for high-technology products is often distinct from the supply and demand for service offerings for such products. Although there may be intense competition in the product sales market⁴, competition for the service of a manufacturer's

⁴ Such competition may not be intense because of the market imperfections mentioned in the Ninth Circuit's

(Continued on following page)

product is at least equally intense. This interbrand service competition constitutes a separate market because, taking into consideration prices, quality and similarity of use of other products, there is no reasonably interchangeable substitute for the service of the product. Under the *duPont* standard, a separate market for support services exists because it is the smallest definable market in which a firm with market power profitably can exploit customers.

Application of the *duPont* standard to Grumman's experience with the servicing of Data General computers results in the conclusion that the servicing of Data General computers is a relevant market for an antitrust analysis. Application of the *Brown Shoe* criteria leads to the same conclusion.

A. Industry and Public Recognition.

The high-technology industry and consumers recognize separate markets for the support service and maintenance of many high-technology products. For example, vendors of support services for Data General equipment advertise their services in specialty magazines that are marketed solely to consumers who own Data General products. These vendors do not advertise this service

(Continued from previous page)

opinion. For example, a certain computer or copier brand may be required for a certain application, reliable comparative information about maintenance costs may not be available to or used by consumers, or purchase of hardware and hardware maintenance within a large organization may be done by different individuals with different objectives.

offering to consumers who own different manufacturers' products. Similarly, service consumers regularly acknowledge that they look to vendors who sell service for their product, rather than manufacturers of other product brands, in selecting service providers.

B. Characteristics and Uses.

The maintenance of specific high-technology products has peculiar characteristics and uses. For example, servicing Data General computer equipment requires specialized skills and knowledge specific to Data General equipment. A field engineer trained to service Data General's computer products could not be expected to service another manufacturer's computer products without extensive retraining. Likewise, servicing Data General computers requires maintaining a large inventory of spare parts which can be used only in Data General computers. Maintenance of high technology products has peculiar characteristics because of the highly technical, specialized differences between different manufacturers' products. For example, competing brands of high technology equipment have different designs, operating systems, peripheral interfaces, protocols and components.

C. Unique Production Facilities.

The maintenance of high-technology equipment typically requires unique production facilities. The most important of these facilities are a large inventory of spare parts and specially trained personnel. For example, a company providing nationwide maintenance on Data General computers must maintain a multi-million dollar

inventory of spare parts and complete, working computers for testing, analyzing and training. Maintaining high-technology products often also requires specialized software diagnostics. All these facilities would be of no use in selling maintenance for another manufacturer's products.

D. Distinct Customers.

The customers for maintenance of specific manufacturer's high technology products are distinct. A business that owns only non-Data General computers will not consider purchasing service for Data General computers. Thus, service vendors of a particular manufacturer's products focus their marketing activities on businesses known to own that manufacturer's products. For instance, vendors of Data General support services advertise in periodicals such as *Focus* and *DG Review* which are directed solely to users of Data General equipment.

E. Distinct Prices.

Prices for maintaining a specific manufacturer's high-technology products are distinct and specific to that manufacturer's products. For example, Grumman and its competitors in the market for servicing Data General equipment specify prices for maintaining a specific Data General computer model based on the characteristics of the equipment. Those prices do not apply to maintenance contracts for other manufacturers' products.

F. Sensitivity to Price Changes.

Prices charged by a vendor of support services for a particular manufacturer's products are sensitive to price changes by other vendors selling support services for the same manufacturer's products. On the other hand, vendor prices for the service of one manufacturer's products are not sensitive to price changes for service on other brands. The fact that IBM⁵, for example, raises its prices to maintain a certain IBM computer would be irrelevant (and probably unknown) to an owner of equipment manufactured by other than IBM.

G. Specialized Vendors.

Vendors for maintenance of a particular manufacturer's equipment are specialized. For example, although there are several hundred independent service organizations for various high-technology products in the United States, there are only a dozen or fewer that provide nationwide service on Data General's MV series of computers. Vendors are specialized because maintaining a particular manufacturer's products requires specially-trained field engineers and unique inventories of spare parts and tools. Most high-technology manufacturers

⁵ In 1956, IBM entered into a consent decree whereby IBM agreed, among other things, to sell spare parts to independent service organization competitors. *United States v. International Business Machines Corp.*, 1956 Trade Cas. (CCH) ¶68,245 (S.D.N.Y. Jan. 25, 1956). These sales neither affected parts prices in the spare parts markets for other manufacturer's products nor resulted in any economic harm to IBM. Kodak's arguments to the contrary are without theoretical or historical merit.

themselves are specialized vendors of support services for products manufactured for them. They either do not service other manufacturer's products or they merely broker servicing of another manufacturer's products to a service vendor specializing in the other manufacturer's product.⁶

From Grumman's own experience, parts and service offerings for different brands of high-technology products are not reasonably interchangeable and, therefore, a manufacturer can hold significant market power in markets for spare parts sales or service of a particular product without having significant power in the product sales market. Most major manufacturers of computers have their own proprietary operating systems and architectures. Thus, a business owning a computer has a large investment in training employees and in application programs. In many cases, the costs associated with retraining employees and rewriting application programs (or procuring new licenses for a new system) are so great that a change to another brand of computer would be uneconomic. The end result is that manufacturers can often charge supra-competitive prices for support services or spare parts sales despite fierce competition in the product sales market. When faced with competition, Data General has lowered its prices for service as much as 70% off its published list prices. In its litigation against Grumman, Data General has asserted that its profit ranges from 60%-70%.

⁶ Ironically, they almost never subcontract to the other manufacturer but to an ISO specializing in the support of the other manufacturer's equipment.

Grumman utilizes thousands of computers in its operations. Grumman began servicing its own Data General computer equipment because of the poor service quality and high cost of service offered by Data General. Data General, like Kodak, was charging supra-competitive prices for its service offerings. At the time, there were few, if any, alternatives to service of Data General equipment by any company other than Data General. The only brand of service that existed was Data General service. Grumman and other independent service companies that entered the market created interbrand competition by offering their own brands of service.

By servicing its own equipment, Grumman is no longer subject to Data General's supra-competitive pricing practices. Grumman has realized considerable savings on its Data General computer service. Likewise, Grumman has been able to provide service to other consumers at an average savings of approximately 25% below Data General's price umbrella. These costs savings are indicators of Data General's supra-competitive profit in the Data General support services market.

II. THE DECISION OF THE COURT OF APPEALS FOSTERS COMPETITION.

Competition in product sales, product service and spare parts markets should be encouraged. Not even Kodak questions that the competitive nature of product sales markets is beneficial. Encouraging competition in support services and spare parts sales markets is similarly beneficial. In fact, without controls on excessive market power in these markets, the business activities of

computer-dependent companies such as Grumman would be threatened.

Despite the savings that Grumman has achieved in servicing its own computer equipment and the savings that Grumman offers to other Data General computer users, Data General's unchecked market power in the support services market is a threat to Grumman and other consumers. As detailed in the Affidavit of Joseph Mulderig, attached as Appendix A⁷ Data General has used its market power against Grumman, just as Kodak has against respondents, to hinder competition in the support services market.

The decision of the Court of Appeals limits a manufacturer's ability to exclude competition and force consumers to purchase service offerings they do not want. Restraints against the exercise of excessive market power in support service markets should be enforced to provide the consumer the choice of a manufacturer's service offering or the often more versatile, higher quality offerings of an independent service organization. Similarly, the anti-trust laws should be enforced to allow consumers the choice of purchasing a manufacturer's integrated system package or purchasing spare parts, support services or diagnostic software separately. The decision of the Court of Appeals fosters competition by allowing consumers' the freedom to choose.

⁷ This affidavit is part of the file in the case cited in footnote 2. For the convenience of the Court, a copy of this affidavit has been lodged with the Clerk's office.

The exercise of excessive market power in any market should be discouraged. Markets for the sale of support services or spare parts should be no exception; otherwise, consumers' freedom of choice is unduly threatened.

CONCLUSION

The application of the antitrust laws is not dangerous. To the contrary, consumer choice encourages quality offerings in the marketplace. Although Grumman is a major manufacturer itself, Grumman favors competition in support services, spare parts sales and product sales markets. A consumer's interest in open competition in all markets, including support services and spare parts markets, is important to the growth of our nation's economy.

For the foregoing reasons, the decision of the Court of Appeals should be affirmed.

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Dated: September 20, 1991